

AR40

Glenayre
electronics

ANNUAL REPORT 1986



Financial Highlights and Five Year Review

for the years ended September 30

(thousands of dollars, except per share data, ratios and statistical data)

Operations Data	1986	1985	1984	1983	1982
Sales	\$23,062	\$21,379	\$18,433	\$15,507	\$12,685
Gross Profit	9,928	7,241	8,342	6,906	5,667
Research and Development	4,043	3,422	2,993	2,558	2,123
Net Earnings before Income Taxes & Extraordinary Item	4,056	993	2,440	2,644	2,047
Net Earnings	2,250	1,901	2,137	1,830	1,373
Dividends Paid	75	74	39	23	47
Capital Expenditures (including goodwill)	482	2,582	4,470	3,347	721
Financial Data					
Working Capital	\$14,917	\$12,893	\$12,620	\$11,247	\$ 4,298
Fixed Assets – Net	6,805	7,080	6,667	2,749	1,008
Long-term Debt	–	43	173	237	338
Shareholders' Equity	23,742	21,471	19,486	14,718	4,830
Ratio and Percentages					
Gross Profit as % of Sales	43.0%	33.9%	45.3%	44.5%	44.7%
Net Operating Earnings as % of Sales	9.0%	3.9%	10.9%	11.8%	10.8%
R & D as % of Manufactured Product Sales	18.8%	21.2%	17.6%	16.5%	16.7%
Current Ratio	4.9:1	3.5:1	2.7:1	4.0:1	2.3:1
Per Common Share Data					
Earnings per Share (basic)	\$0.60	\$0.51	\$0.59	\$0.64	\$0.60
Book Value per Share	6.34	5.77	5.27	4.31	2.06
Market Price Range – High	10 ⁷ / ₈	8 ¹ / ₈	12 ⁵ / ₈	14 ¹ / ₂	–
– Low	5 ¹ / ₂	4.95	6 ³ / ₄	9 ¹ / ₂	
Statistical Data					
Number of Common Shares Outstanding (average)	3,734,433	3,703,779	3,601,402	2,856,030	2,286,575
Number of Common Shareholders	610	700	742	898	164
Number of Employees	239	214	191	175	164

Annual General Meeting

The Annual General Meeting of the Shareholders will be held on Thursday, January 22, 1987 at 11:00 am in the Garibaldi Room of the Four Seasons Hotel, 791 West Georgia Street, Vancouver.

FRONT COVER: Shaded areas denote the international marketplace served by Glenayre.

Corporate Profile

Since the late 1970s Glenayre Electronics has gained a key position in the North American mobile communications market. Glenayre's business operations in the past year have resulted in further consolidation of this market, as well as extension of our established product lines into targetted offshore markets.

The acquisition of WR Communications allowed for the introduction of new radio products to all our markets. This additional capability, together with our in-house developments of voice and data products, positions Glenayre for sales expansion into adjacent mobile communications sectors.

Research and development as well as the growth of our distribution channels are key characteristics of the company's operation. During the 1985/1986 fiscal year we spent 18.8% of sales on research and development. A significant market position is established in the People's Republic of China, as well as strengthening our position in Canada, the U.S.A. and Mexico.

Also during the past year, computer aided design and automated test equipment was introduced at our main plant, as well as facilities for certification testing of products to meet North American and International standards.

Glenayre's corporate head office, with over 230 employees, is located in Vancouver, B.C., Canada. All marketing resources, engineering design laboratories, production, and test facilities are also located in the corporate office. Regional sales offices cover Canada and the U.S.A. Sales representatives and agents are located in the U.S., Mexico, South America, the Middle East, and Australia.



Report to Shareholders

Fiscal 1986 has been a year of substantial progress and achievement for Glenayre. Company sales and profits rebounded significantly from 1985. We met or exceeded most of our 1986 goals. The growth of Glenayre manufactured products over the past year rose from \$16,154,000 to \$21,265,000, an increase of 31.6%. Earnings before extraordinary item increased from \$835,000 to \$2,076,000, an increase of 148.6%. The order backlog was maintained at the previous year's level, in spite of the increased sales. Our gross profits improved from 33.9% to 43.0%.

The major priorities targetted for 1986 were to broaden our business profile and customer base to include base station transmitters and receivers, paging transmitters and messaging equipment, covering wider market sectors from our original base of mobile telephone equipment, and paging switching terminals. We have also increased our customer base, strengthened our business relationships with major customers, and solidified our long term business position. In the messaging business we undertook a major review of our technical, market and support capabilities and have aligned the company to provide the total spectrum of services with in-depth support.

To maintain our product engineering standards, we redesigned and improved the entire line of base stations and repeaters, mountain top repeaters, and paging transmitters, including a new line of power amplifiers obtained in the acquisition of WR Communications. All of these products have passed or are in the approval process for certification by the regulatory authorities of the U.S. Federal Communications Commission (F.C.C.) and in Canada the Department of Communications (D.O.C.). This was a major technical undertaking and cost, and should position us well in this market. Our paging terminals are now an accepted product in both the U.S. and Canadian markets, and in Hong Kong, where our first terminal just went into operation.

A new product line which has been developed, or is well on its way to completion, is our line of UHF and VHF radios. Specifications have been developed for a generic line of radios, and new control heads, which on completion, will include 800 mHz and special cellular applications. The primary concept of this line of radios is to provide full data and voice capability at an economical cost. We anticipate that these products will extend the life of our mobile telephone terminal market and enhance our position in international markets. The market introduction of these products is expected in the second and third quarters, with further added releases over the following 18 months.

We encountered difficulties with the software for the larger types of Message Manager systems. We have four trial systems operating in the U.S. and Canada with a capacity of 450 customers. On attempting to double this capacity, we encountered some instability, however recent tests appear favorable. Extensive work and market research has been done regarding the application of these designs to the "corporate" message markets. This could open a large market if we are successful in this development.

Our policy has been to remain constantly alert to opportunities to acquire, or joint venture, products that can expand our market offerings. Several interesting proposals are presently under active consideration, the most significant being the acquisition of the communications division of a well-known national distributor of communication products. No agreements have been finalized at this time, however if it is established that Glenayre's "value added" technology and manufacturing can increase our mutual sales and profitability, then this could be a good move for both companies. Because of third party participation, these negotiations have been protracted, however we hope to resolve this early in the second quarter.

Prior to the sale of our railway technology to Dynamic Sciences Limited (DSL), we initiated an R&D program which would allow for the application of the brakes to the rear of the train at the same time that the locomotive is put into an emergency stop. This feature would tremendously increase the safety of all emergency stops, and an undetermined number of lives could be saved. There would also be a tremendous decrease in the costs of the derailments that usually accompany an emergency stop. We are pleased to announce that DSL have completed, and successfully tested this feature, on both the CNR and CPR. Transport Canada is presently conducting hearings regarding the application of this product to all Canadian railways. There will not be an early decision, however we will probably be favored with an approval late in the year.

In addition to increased R&D effort, we have expanded our efforts in sales and market development. Costs have increased significantly from \$1,755,000 to \$2,674,000, an increase of 52.4%. Markets have been established or reactivated in Mexico, Chile, Salvador, Hong Kong, and China. The latter has been particularly expensive. Results have been slow by our standards, however in comparison with other companies, we understand that our progress has been rapid and impressive. Five mobile radio telephone systems are operating in China. A major delegation is expected in December to finalize plans for our first Chinese joint venture. This will be a slow start, beginning with assembly of partially completed control heads. The terminals and peripherals will be built in Vancouver. Hopefully we can announce further completed contracts before our annual meeting. In addition to the December delegation, four prominent Chinese groups were entertained at our plant in the past year.

Our continued high investment in R&D, market development, capital equipment and professional staff, should position us to re-establish our historic growth and profit patterns. In this last year these expenditures included a computer aided design system, laboratory equipment and the necessary staff training to use these new techniques. We also increased the size and quality of our sales staff.

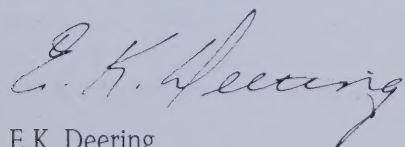
Our plans have been structured to respond to new opportunities, and are deliberately flexible to adjust to any economic factors which may impact our sales in the various market sectors. The balance sheet has been kept strong, so that we can respond. However, it is our intention to take an aggressive stance, as long as the economic climate is favourable.

There appear to be significant opportunities for our new products in rural communications, particularly in the international market. Our studies show not only a great need for our products, but also that high priority is being placed by all governments on improving rural communications in underdeveloped countries.

Fiscal 1986 was one of substantial growth and increased productivity in every facet of our business. It was a year of improved margins and profitability.

Our company is indebted to our customers for their loyalty, cooperation and support. During this last year Glenayre paging systems were judged the best in the business, but without such customer support and dedicated effort by our entire staff, such facts and the results reported above would not have been possible.

On behalf of the Board, I thank you.

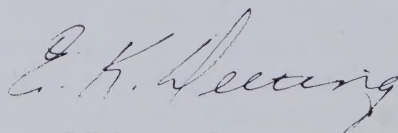
A handwritten signature in dark ink, appearing to read "E.K. Deering".


E.K. Deering
Chairman, President and
Chief Executive Officer
December 22, 1986

Consolidated Balance Sheet

	As at September 30th 1986	As at September 30th 1985
ASSETS		
Current Assets		
Cash and short-term deposits	\$ 5,880,000	\$ 5,911,000
Accounts receivable	6,021,000	5,710,000
Inventories (Note 3)	6,718,000	6,389,000
Prepaid expenses	139,000	91,000
Total Current Assets	18,758,000	18,101,000
Agreements Receivable (Note 4)	368,000	—
Fixed Assets (Note 5)	6,805,000	7,080,000
Investment Tax Credits Recoverable	1,266,000	—
Goodwill and Other Assets (Note 6)	1,333,000	1,767,000
	\$28,530,000	\$26,948,000
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Accounts payable and accrued liabilities	\$ 3,582,000	\$ 4,076,000
Income taxes payable	103,000	117,000
Current portion of long-term debt	—	1,015,000
Deferred income taxes	156,000	—
Total Current Liabilities	3,841,000	5,208,000
Agreement Payable	—	226,000
Long-Term Debt	—	43,000
Deferred Income Taxes	947,000	—
Total Liabilities	4,788,000	5,477,000
Shareholders' Equity		
Share capital (Note 7)	11,714,000	11,618,000
Contributed surplus	163,000	163,000
Retained earnings	11,865,000	9,690,000
Total Shareholders' Equity	23,742,000	21,471,000
	\$28,530,000	\$26,948,000

On behalf of the Board of Directors


E.K. Deering, Director

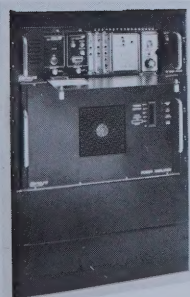

H.W. Scott, Director

Consolidated Statement of Earnings

	Year ended September 30th 1986	Year ended September 30th 1985
Sales	\$23,062,000	\$21,379,000
Expenses		
Cost of goods sold	13,134,000	14,138,000
Research and development (Note 8)	4,043,000	3,422,000
Less: Investment tax credits (Note 2)	(1,899,000)	—
Administrative and selling expenses	3,276,000	2,512,000
Depreciation and amortization	944,000	837,000
Interest income	(492,000)	(523,000)
Total Expenses	19,006,000	20,386,000
Earnings Before Income Taxes & Extraordinary Item	4,056,000	993,000
Income Taxes (Note 9)		
Current	703,000	132,000
Deferred	1,277,000	26,000
Total Income Taxes	1,980,000	158,000
Earnings Before Extraordinary Item	2,076,000	835,000
Extraordinary Item (Note 12)	174,000	1,066,000
Net Earnings	\$ 2,250,000	\$ 1,901,000
Earnings Per Share		
Before extraordinary item	\$0.56	\$0.23
After extraordinary item	\$0.60	\$0.51
Weighted Average Number of Shares Outstanding		
During the Year	3,734,433	3,703,779

Consolidated Statement of Retained Earnings

	Year ended September 30th 1986	Year ended September 30th 1985
Retained Earnings – Beginning of Year	\$ 9,690,000	\$ 7,863,000
Net Earnings	2,250,000	1,901,000
Dividends	(75,000)	(74,000)
Retained Earnings – End of Year	\$11,865,000	\$ 9,690,000



Consolidated Statement of Changes in Cash Resources

	Year ended September 30th 1986	Year ended September 30th 1985
Cash Derived From		
Operations (Note 10)	\$ 4,141,000	\$ 2,779,000
Changes in Working Capital (Note 10)	(2,055,000)	603,000
	2,086,000	3,382,000
Cash Derived From (Applied To) Investing Activities		
Fixed Asset Acquisition	(482,000)	(775,000)
Acquisition of WR Communications Ltd.		
Goodwill	—	(278,000)
Net long-term assets	—	(1,437,000)
Investment Tax Credits Recoverable	(1,266,000)	—
Agreements Receivable	(368,000)	—
Agreements Payable	(226,000)	—
Other	247,000	4,000
	(2,095,000)	(2,486,000)
Cash Derived From (Applied To) Financing Activities		
Repayment of long-term debt	(43,000)	(104,000)
Issue of shares	96,000	158,000
Dividends paid	(75,000)	(74,000)
	(22,000)	(20,000)
Net Increase (Decrease) In Cash Resources	(31,000)	876,000
Cash Resources – Beginning of Year	5,911,000	5,035,000
Cash Resources – End of Year	\$ 5,880,000	\$ 5,911,000

Auditors' Report

To the shareholders of Glenayre Electronics Ltd.

We have examined the consolidated balance sheet of Glenayre Electronics Ltd. as at September 30, 1986 and the consolidated statements of earnings, retained earnings and changes in cash resources for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at September 30, 1986 and the results of its operations and the changes in its cash resources for the year then ended in accordance with generally accepted accounting principles applied, except for the change in the method of accounting for investment tax credits as required by the Canadian Institute of Chartered Accountants and as explained in Note 2 to the financial statements, on a basis consistent with that of the preceding year.

Spicer MacGillivray

Spicer MacGillivray
Chartered Accountants
Vancouver, Canada
December 4, 1986

Notes to the Consolidated Financial Statements

1. Summary of Accounting Policies

These financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada, and conform in all material respects with International Accounting Standards, except that these financial statements do not reflect the impact of general price level changes. The more significant policies are outlined below.

(a) Consolidation:

The consolidated financial statements include the accounts of Glenayre Electronics Ltd. and its wholly-owned subsidiary Glenayre Electronics Inc. after elimination of inter-company accounts and transactions.

(b) Foreign Currency Translation:

The accounts of Glenayre Electronics Inc. have been translated into Canadian dollars as follows: monetary assets and liabilities at the exchange rate in effect at the balance sheet date, non-monetary items at the exchange rate in effect when they were acquired, and revenue and expenses (other than depreciation and amortization) at the exchange rates during the year. The resulting gains or losses on translation are included in the results of operations.

(c) Revenue Recognition:

Revenue is recognized at the time the goods are shipped or services are provided to customers.

(d) Inventories:

Raw materials are valued at the lower of the average cost of materials purchased and replacement cost. Work in progress and finished goods are valued at the lower of cost and net realizable value.

(e) Fixed Assets:

Fixed assets are stated at cost. Depreciation is based on the expected useful lives of the respective assets as follows:

	Method	Rate
Computer software	Declining Balance	50% and 100%
Computer hardware	"	30%
Machinery and furniture	"	20%
Building	Straight Line	4%

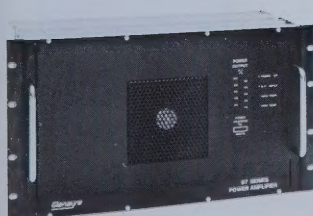
Tooling is amortized on a per unit basis calculated on the estimated future sales of the product line.

(f) Goodwill and Other Assets:

Goodwill resulting from corporate acquisitions and licence agreement are amortized on a straight line basis over 10 years. (Note 6)

(g) Income Taxes:

The company follows the tax allocation method in providing for income taxes. Under this method deferred income taxes arise because certain income and expense items, principally depreciation, amortization and government grants, are reported in the financial statements in years different from those reported for income tax purposes. Deferred income taxes are provided on these timing differences as they arise at current tax rates.



2. Change in Accounting Policy – Investment Tax Credits

The Canadian Institute of Chartered Accountants has issued a new standard in accounting for Investment Tax Credits which must be incorporated into the company's accounting policies during the 1986 fiscal year.

Under this method, investment tax credits relating to the acquisition of fixed assets are recorded as a reduction from the cost of the assets acquired and those relating to research and development expenses are recorded as a reduction in research and development expenses. In prior years, the company utilized investment tax credits to reduce the provision for income taxes, resulting in a lower effective tax rate. This current year change in accounting policy has resulted in a \$129,000 increase in net earnings over what the company would have recorded using the prior year's accounting policy for investment tax credits.

3. Inventories

	1986	1985
Raw materials	\$3,844,000	\$3,429,000
Work in process	2,234,000	2,130,000
Finished goods	640,000	830,000
	\$6,718,000	\$6,389,000

4. Agreements Receivable

Agreements receivable represent contracts between the company and its customers. These contracts bear interest at prime plus 1% and the company maintains title to the equipment until the contract has been paid in full.

	1986	1985
Agreements receivable	\$ 580,000	\$ —
Less: Current portion (included in accounts receivable)	212,000	—
	\$ 368,000	\$ —

5. Fixed Assets

	1986	1985
Land	\$1,492,000	\$1,492,000
Building	3,761,000	3,743,000
Machinery, furniture and tooling	4,503,000	4,047,000
	9,756,000	9,282,000
Less accumulated depreciation	(2,951,000)	(2,202,000)
	\$6,805,000	\$7,080,000

6. Goodwill and Other Assets

	1986	1985
Goodwill	\$1,594,000	\$1,594,000
Licence Agreement	300,000	300,000
Other	2,000	228,000
	1,896,000	2,122,000
Less accumulated amortization	(563,000)	(355,000)
	\$1,333,000	\$1,767,000

7. Share Capital

- (a) Authorized:
10,200,000 common shares without par value.
- (b) Issued Shares

	Issued Shares	Amount
Balance – September 30, 1984	3,700,981	\$11,460,000
Issued during the year:		
Cash	13,165	58,000
VMX Licence Agreement	10,000	100,000
Balance – September 30, 1985	3,724,146	11,618,000
Issued during the year:		
Cash	21,926	96,000
Balance – September 30, 1986	3,746,072	\$11,714,000

- (c) Shares reserved for issue:

	September 30th 1986	September 30th 1985
Employee Stock Plans	324,109	346,035

Options for 86,000 shares have been granted under Employee Stock Plans at prices ranging from \$6.88 to \$7.32 per share, exercisable until 1990.

- (d) Shares Held in Escrow

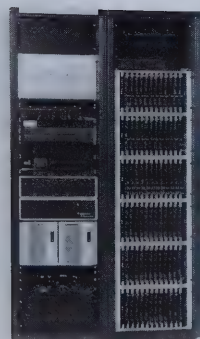
	September 30th 1986	September 30th 1985
Subject to terms approved at the initial issue of shares to the public in April 1983	—	582,065
Under employee share purchase arrangements	41,244	47,077
Total	41,244	629,142

8. Research and Development

- (a) Company Policy
All research and development expenses are charged against earnings in the year they are incurred.
- (b) Summary

	1986	1985
Company funded expenses	\$4,352,000	\$3,733,000
Government funded expenses	1,145,000	647,000
Contact Research	—	133,000
Total research and development	\$5,497,000	\$4,513,000

Company funded expenses above differs from that shown in the earnings statement due to the inclusion of depreciation expenses in the above figures (1986 – \$309,000; 1985 – \$311,000).



GL 3000 DC
Voice Retrieval and
Paging System

9. Income Taxes

The company's income tax rate for the current fiscal year is 46.7% (1985 – 46.4%). The reported income tax expense for 1986 does not reflect this rate primarily because of the non-deductibility of a portion of the goodwill amortization expense. The reported income tax expense for 1985 does not reflect a rate of 46.4% primarily because of claiming income tax credits. (Note 2)

As at September 30, 1986 the company has unrecognized tax benefits originating from the purchase of the WR Communications Ltd. group which are available to reduce future income taxes, as follows:

Date of Expiry	Investment Tax Credits	Loss Carried Forward	Research and Development Expenses
September 30, 1992	\$159,000	\$ —	\$ —
September 30, 1993	800,000	—	—
Post September 1993	—	1,280,000	2,410,000
	\$959,000	\$1,280,000	\$2,410,000

10. Statement of Changes In Cash Resources

	1986	1985
Cash derived from operations		
Net earnings before extraordinary item	\$2,076,000	\$ 835,000
Add non-cash items		
Depreciation & Amortization	944,000	837,000
Deferred Tax	947,000	26,000
Loss on sale of fixed assets	—	15,000
Extraordinary Item	174,000	1,066,000
	\$4,141,000	\$2,779,000
Cash derived from (applied to) changes in working capital		
Accounts receivable	\$ (311,000)	\$2,329,000
Inventory	(329,000)	(142,000)
Accounts payable and accrued liabilities	(494,000)	(3,107,000)
Current portion of long term debt	(1,015,000)	950,000
Income tax	142,000	775,000
Other	(48,000)	(202,000)
	\$(2,055,000)	\$ 603,000

11. Segmented Information

The company's markets presently include Canada, United States, and other foreign countries including Mexico, the Peoples' Republic of China, Saudi Arabia, Chile, Columbia, Australia and Hong Kong.

	Glenayre Electronics Ltd.	Glenayre Electronics Inc.	Inter- Company Eliminations	Total
1986 SALES				
<i>(thousands of dollars)</i>				
Sales – Canada	\$ 8,844	\$ –	\$ –	\$ 8,844
– United States	–	12,172	–	12,172
– Other	2,046	–	–	2,046
Transfer between Segments	10,344	–	(10,344)	–
Total sales	\$21,234	\$12,172	\$(10,344)	\$23,062
Net earnings	\$ 1,850	\$ 400	\$ –	\$ 2,250
Total Assets	\$25,485	\$ 3,555	\$ (510)	\$28,530

	Glenayre Electronics Ltd.	Glenayre Electronics Inc.	Inter- Company Eliminations	Total
1985 SALES				
<i>(thousands of dollars)</i>				
Sales – Canada	\$ 3,114	\$ –	\$ –	\$ 3,114
– United States	–	16,096	–	16,096
– Other	2,169	–	–	2,169
Transfer between Segments	8,299	–	(8,299)	–
Total sales	\$13,582	\$16,096	\$ (8,299)	\$21,379
Net earnings	\$ 1,874	\$ 27	\$ –	\$ 1,901
Total Assets	\$24,566	\$ 4,655	\$ (2,273)	\$26,948

12. Extraordinary Item

	1986	1985
Gain on sale of DIGITAIR marketing and patent rights	\$ –	\$1,213,000
Realization of loss carry forward originating from the purchase of WR Communications Ltd. Group (Note 9)	174,000	–
Less related income taxes	–	(147,000)
	\$174,000	\$1,066,000

13. Subsequent Events

Several joint ventures and/or acquisitions are currently under active consideration, the most significant of which is the communications division of A.C. Simmonds Ltd., a Canadian electronics distributor. No agreements have been made at this time.



Corporate Information

Directors

B.H. Brady*
*President of
Brink Hamilton Enterprises Ltd.
Vancouver, B.C.*

J.W. Chisholm
*President of
Boarshead Development Ltd.
Vancouver, B.C.*

E.K. Deering*
*Chairman, President &
Chief Executive Officer*

G.H.D. Hobbs*
*Private Investor
Vancouver, B.C.*

D.G. Melvin
*McTaggart, Ellis & Co.
Vancouver, B.C.*

H.W. Scott
*Private Investor and former
Plant Manager*

W.R. Wyman
*Chairman
Pemberton Houston Willoughby
Bell and Gouinlock Inc.*

**Member of Audit Committee*

Officers

E.K. Deering
*Chairman, President &
Chief Executive Officer*

P.M. Bradley
*Exec. Vice President &
General Manager*

J.F. Francis
Vice-President Manufacturing

M.P. Hodson
Vice-President Engineering

T.A. Kordyback
*Controller & Assistant
Secretary*

D.G. Melvin
Secretary

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Representation

Marietta, Georgia
Chicago, Illinois
Rochester, New York
Eugene, Oregon
Pinehurst, Texas
Toronto, Ontario

Auditors

Spicer MacGillivray
Vancouver, B.C.

Transfer Agent and Registrar Bank

The Canada Trust Company
Vancouver, B.C.

The Royal Bank of Canada

Exchange Listing

Toronto Stock Exchange "GLN T"



Glenayre
electronics